

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Illinois Power Company

)

Docket No. ER01-2999-000

**COMMENTS OF THE
ILLINOIS COMMERCE COMMISSION**

Pursuant to Rule 211 of the Commission's Rules of Practice and Procedure, 18 C.F.R. 385.211, the Illinois Commerce Commission ("ICC") hereby submits its comments in the above-captioned proceeding in response to a filing submitted by Illinois Power Company ("IP") on August 31, 2001, wherein IP proposed rate changes, and particularly increases, for the base rate component and Schedule 1 component of IP's electric transmission rates ("IP's Rate Filing"). The ICC respectfully requests that the Commission: 1) reject IP's levelized ratemaking proposal; 2) initiate a hearing and direct its Staff to investigate the justness and reasonableness of IP's proposed rates; and 3) suspend IP's proposed rates for the maximum period allowed pending their investigation.

I. INTRODUCTION AND BACKGROUND

Pursuant to a settlement agreement among the Midwest Independent System Operator, Inc. ("MISO"), certain transmission owners in the MISO and the Alliance Companies, the Alliance Companies were required to file transmission rates for the Alliance Regional Transmission Organization ("ARTO") no later than 120 days prior to the transmission service

date.¹ Consequently, the Alliance Companies submitted their proposed transmission rates for the ARTO on August 31, 2001, fifteen days late. In their filing, the Alliance Companies provide rate schedules applicable to a rate structure that provides for zonal rates for loads in each ARTO zone, and a single regional through and out rate. The largest component of each of the ARTO's zonal rates, the zonal facilities charge, will be comprised of Illinois Power's and the other Alliance Companies' individual system rates (existing rates for five of the Alliance Companies and proposed new rates for the other five companies).

On August 31, 2001, simultaneously with the Alliance Companies' rate filing, IP filed proposed revisions to its electric transmission rates to establish new base transmission rates and new rates for Schedule 1 ancillary service. Notably, IP's transmission rate filing is voluntary. No aspect of FERC's RTO policy or the Alliance RTO proposal required IP to make its rate filing. IP states that it seeks to adjust IP's cost of service for zonal rates, rather than rely on previous system rates.²

IP further states that it seeks transmission rate changes in this proceeding due to: "increases in transmission plant in rate base, increases in transmission expenses, and a greater percentage allocation of certain costs to the transmission function due to the absence of a generation line of business."³ For example, IP states that it has seen an increase in its transmission plant of more than \$10 million dollars and a greater than 20% increase in its operations and maintenance expenses.⁴ In addition, IP states that the divestiture of its generation

¹ See, *Alliance Companies, et al.*, 96 FERC ¶ 61,052, slip op. at 20-21 (2001); *Illinois Power Company, et al.*, 95 FERC 61,183 (2001), *reh'g denied*, 96 FERC ¶ 61,026 (2001).

² IPC-1 at 4, ln. 22.

³ Transmittal Letter at 3.

⁴ *Id.* at 5, ln. 12.

assets to an affiliate has resulted in certain costs, such as corporate administrative and general expenses, now being spread over fewer lines of business, in particular the transmission function.⁵

The proposed rates that IP seeks will allow IP to recover a total of \$38.3 million in base rate revenues for each year of the ARTO transition period, a 54.8% increase relative to the revenues that would be collected under IP's current base transmission rates that the Commission approved on October 12, 2000.⁶ Such an increase in revenue requirements, in conjunction with IP's proposed new billing determinants, leads to an increase of 47.3% in the transmission rate that IP proposes to charge (from \$597/Mw-mo to \$879.42/Mw-mo).⁷ Additionally, IP seeks to increase the revenue requirement associated with ancillary service Schedule 1 to \$7.8 million, a 136% increase relative to that currently authorized.⁸

Finally, in addition to the transmission rate base additions, transmission expense increases and increased allocation of costs to the transmission function, IP (1) seeks a rate of return on common equity of 14.00%;⁹ and (2) proposes to calculate rates on a gross levelized basis, rather than using the traditional depreciated non-levelized method.¹⁰

The ICC respectfully requests that the Commission reject IP's proposal to utilize the levelized ratemaking methodology. As explained *infra*, acceptance of IP's levelized ratemaking proposal would result in artificially high transmission rates, and an unjust and unreasonable windfall to IP at the expense of transmission ratepayers. In addition, the ICC respectfully requests that the Commission initiate a hearing to investigate the justness and reasonableness of

⁵ *Id.* at 5, ln. 4.

⁶ IPC-6, Statement BK, Schedule 1, at 1, ln. 22. *See also, Illinois Power Company*, 93 FERC ¶61,036 (Oct. 12, 2000)(authorizing IP's current rates).

⁷ *Id.*, Statement BL, at 1, ln 12.

⁸ IPC-1 at 5, ln. 20-22.

⁹ Transmittal Letter at 10.

¹⁰ IPC-4 at 7, ln. 10.

IP's proposed transmission rates, and that the Commission suspend IP's proposed rate increases for the maximum time permitted pending their investigation.

The ICC makes this latter request although it declines to address, herein, aspects of IP's transmission rate filing other than IP's request to utilize levelized rates. In particular, the ICC will not herein address: (1) the appropriate rate of return on equity; (2) the appropriateness of an increase to IP's transmission rate base; (3) the appropriateness of an increase to IP's transmission expenses; or (4) IP's proposal to modify the allocation of costs to the transmission function. As explained *infra*, the ICC is evaluating similar testimony that has been filed by IP in a proceeding on IP's Delivery Services Tariff that is currently pending before the ICC.¹¹ In that case, the ICC is investigating questions and concerns raised by intervenors on numerous aspects of IP's filing that IP supports with evidence similar to that contained in IP's present filing before the Commission.

II. DISCUSSION

A. **The Commission should reject IP's proposal to switch from depreciated non-levelized ratemaking to gross-levelized ratemaking.**

In this transmission rate proceeding, IP seeks to increase its base transmission rate revenue requirement to \$38,317,102, a 54.8% increase relative to IP's current transmission revenue requirement. In addition, IP seeks to increase the revenue requirement associated with ancillary service Schedule 1 to \$7.8 million, a 136% increase relative to that currently authorized by the Commission. In support of its proposed revenue requirement, IP provides the testimony of Mr. Alan C. Heintz (IPC-4).

¹¹ Proposed revisions to delivery services tariff sheets and other sheets, *Illinois Power Co.*, ICC Docket No. 01-0432 (filed June 1, 2001).

Citing Order 2000, Mr. Heintz employs the levelized rate methodology to derive IP's proposed revenue requirements.¹² In Orders 2000 and 2000-A, the Commission stated that the use of levelized rates *may* be appropriate in the RTO context.¹³ The Commission explained that one of the main reasons for allowing the use of levelized rates is to *address concerns of reduced utility revenues* associated with RTO formation.

The use of the levelized rate methodology in the context of IP's rate request, however, is inappropriate because the ARTO rate design being advanced by the Alliance Companies, and supported by IP, already contains provisions designed to address the issue of lost revenues due to membership in an RTO. In its August 31, 2001 rate filing, the Alliance Companies present the testimony of J. Stephen Henderson.¹⁴ In his testimony, Mr. Henderson states that the intent of the Alliance RTO regional rate structure is to collect the amount of revenue lost as a result of the elimination of rate pancakes.¹⁵ The ARTO rate structure recovers these lost revenues through the application of a zonal transmission adjustment ("ZTA"),¹⁶ a super-regional rate adjustment ("SRA")¹⁷ and a regional through and out rate ("RTOR").¹⁸ The ZTA, SRA and RTOR ensure that each transmission owner is made whole with regard to transmission revenues lost as a result of joining the RTO. Accordingly, the use of levelized rates by IP in this proceeding violates the basic assumption underlying the Commission's discussion of levelized rates in Orders 2000 and 2000-A, i.e., that the elimination of rate pancaking resulting from RTO formation would result in lost utility revenues.

¹² *Id.* at 7, ln. 4.

¹³ Order No. 2000, *Regional Transmission Organizations*, 65 Fed. Reg. 809, slip op. at 31,194 (Jan. 6, 2000), FERC Stats. and Regs. ¶ 31,089 (1999), *order on reh'g*, Order No. 2000-A, 65 Fed. Reg. 12,088, slip op. at 31,386 (Mar. 8, 2000), FERC Stats. and Regs. ¶ 31,092 (2000).

¹⁴ Wholesale Electric Transmission Rate Filing, Exhibit JSH-1, *Alliance Companies, et al.*, Docket No. RT01-88-006 (filed Aug. 31, 2001).

¹⁵ JSH-1 at 6, ln. 10.

¹⁶ *Id.*, ln. 16.

Furthermore, in numerous opinions, the Commission has placed an obligation on the utility wishing to switch from non-levelized to levelized rates to prove that the utility's proposal to utilize levelized rates to recover capital costs is reasonable when compared to the method used by the utility to recover capital costs in the past.¹⁹ IP, however, fails to provide any substantial evidence to justify the switch from non-levelized rates beyond the Commission's general statements in Orders 2000 and 2000-A that the use of levelized rates *may* be appropriate in the RTO context. Instead, IP attempts to justify its use of levelized rates merely by citing two Commission orders and the Planning and Expansion Characteristic of an RTO as outlined in the Commission's Order 2000.²⁰ As explained, neither the Commission orders that IP cites nor Order 2000's Planning and Expansion Characteristic constitutes a sufficient basis to justify IP's use of levelized rates.

First, citing *Maine Public Service Co.*,²¹ IP argues that Commission precedent indicates that where significant transmission additions or upgrades are planned for the future, levelized rates may be appropriate. However, the Commission denied Maine PSC's use of levelized rates because Maine PSC's transmission facilities were over 50% depreciated and Maine PSC had failed to provide evidence of plans for significant transmission upgrades.²² There are similarities between Maine PSC and IP in this filing. For example, like Maine PSC, IP has failed to provide any evidence of any major planned transmission additions or upgrades. Instead, IP states: "The Alliance Companies *anticipate* significant transmission upgrades and additions once the Alliance

¹⁷ *Id.* at 8, ln. 3.

¹⁸ *Id.* at 9, ln. 2.

¹⁹ See, *American Electric Power Service Corp.*, 88 FERC ¶61,141 at ¶61,442 (1999); *Allegheny Power Service Corp.*, 85 FERC ¶61,275 at ¶62,117 (1998); *Kentucky Utilities Co.*, 85 FERC ¶61,274 at ¶62,100 (1998).

²⁰ Transmittal Letter at 6.

²¹ *Maine Public Service Co.*, 85 FERC ¶61,412 (1998).

²² *Id.* at ¶62,564.

RTO is operational.”²³ While incentives for transmission construction may be appropriate once the Alliance RTO becomes operational and takes responsibility for the planning and expansion function, the Commission should not reward IP upfront in this rate filing by increasing rates for use of existing facilities on the basis that new facilities *might be* constructed in the future.

In addition, like *Maine PSC*, IP’s transmission plant is highly depreciated. Data provided by IP shows that gross transmission plant is \$241 million.²⁴ IP’s transmission accumulated depreciation is over \$115 million.²⁵ Therefore, IP’s own numbers show that its facilities are nearly 50% depreciated, and that percentage may be higher if IP’s gross transmission plant is determined by the Commission to be lower than that advanced by IP. As the Commission recognized in Order 2000 and *Maine PSC*, in situations where there is a significant amount of accumulated depreciation, levelized rates provide a utility with increased revenues by producing higher rates than a non-levelized approach for the same depreciated investment base.²⁶ Accordingly, if the Commission were to grant IP’s levelized ratemaking request, then IP would effectively be able to recover its accumulated depreciation a second time in rates. In other words, the implementation of levelized rates would result in a windfall to IP of approximately \$115 million dollars to be recovered in a future revenue stream generated by higher transmission rates.

IP further argues that the Commission places a premium on upgrading and expansion of transmission facilities, citing the Commission’s order regarding the electricity crisis in California and the Western United States.²⁷ The circumstances underlying the Commission’s California

²³ Transmittal Letter at 6 (emphasis added).

²⁴ IPC-6, Statement AD, at 1.

²⁵ *Id.*, Statement AE, at 1.

²⁶ Order 2000 at ¶31,193.

²⁷ *Removing Obstacles to Increased Electric Generation and Natural Gas Supply in the Western United States*, 96 FERC ¶61,155, slip op. at 5 (2001)(“California Order”).

Order, however, are significantly distinguishable from present circumstances in IP's service territory. In the Commission's California Order, the Commission made it clear that the provisions adopted to induce the timely completion of transmission enhancements were adopted "due to the extraordinary circumstances surrounding the ongoing imbalances in California's electricity power supply system, as reflected by the severity of the power shortages in the WSCC in general and in California, specifically."²⁸ The Commission's actions in the California Order were in response to the need for immediate relief in the West to preserve continued reliable delivery, a problem that does not currently exist in IP's service territory and, consequently, the resolution of which should not be applied as precedent to IP's present filing.

IP also cites the Commission's Planning and Expansion Characteristic of an RTO as reason to grant levelized rates.²⁹ IP's attempt to draw a link between the Commission's requirement that an RTO have the authority to plan and direct necessary transmission upgrades and expansions on the one hand and the use of levelized rates on the other hand is, at best, premature. In Order 2000-A, the Commission stated: "We agree that a transmission owner is entitled to compensation for construction undertaken *at the directive of an RTO*, and we expect that these issues will be resolved systematically by the RTO."³⁰ In this case, however, the ARTO has not given any directive to IP for transmission upgrades and expansions, nor is the ARTO proposing levelized rates on IP's behalf in connection with an RTO-directed transmission facility expansion. Indeed, at this time, the Commission has not even approved the Alliance Companies' proposal for an ARTO expansion and planning protocol.

²⁸ *Id.* at ¶61,670.

²⁹ Transmittal Letter at 6.

³⁰ Order 2000-A at ¶31,381.

In addition, IP argues at length that switching to levelized rates in this proceeding should be accepted because the service that the ARTO will provide is “new service.”³¹ Indeed, Order 2000 states that levelized ratemaking may be appropriate in establishing initial rates under an RTO structure “where an RTO reflects a fresh start with respect to the provision of transmission services.”³² However, Order 2000 specifically cites as “new service” circumstances where “the transmission customers of the RTO may be significantly different than the traditional, captive customers that formerly took transmission service.”³³

Again, these circumstances do not hold for IP in this proceeding. This proceeding is intended to establish the zonal rates for service to loads within IP’s zone of the Alliance RTO. The loads within IP’s zone of the Alliance RTO are, for the most part, the same loads that exist now within IP’s service territory and that existed within IP’s service territory during the test years underlying previous IP rate cases. In short, the ultimate loads to be served in IP’s zone are not significantly different than those previously served by IP’s transmission service. Therefore, IP is not seeking to utilize levelized rates in the context of a “new service” because transmission customers are not “new” as assumed in Order 2000.

IP also supports the increase in transmission rates that will result from switching to levelized ratemaking on the rationale that the detriments of that rate increase for customers will be offset by the benefits that customers will receive under the super regional rate agreement.³⁴ In particular, IP states as follows: “In short, the total cost of delivered energy at the point of consumption should be lower, even if particular pre-existing delivery charges increase.”³⁵ However, contrary to this statement in IP’s transmittal letter, IP witness Shawn E. Schukar

³¹ Transmittal letter at 4.

³² Order 2000, slip op. at 570.

³³ *Id.*

³⁴ Transmittal letter at 5.

testifies: “Illinois Power expects that the single ARTO-wide rate will inevitably and initially cause some transactions to appear more economical under the ARTO rate structure while others will appear less economical.”³⁶ Indeed, the design of the super-regional rate, which includes adjustment factors for the loss of pancaking both within the ARTO and between the ARTO and the Midwest ISO (the ZTA and SRA respectively), will mean that transmission customers who wish to continue buying power from generators within a particular zone will have to pay substantially more for transmission service than they would if there were no super-regional rate. Moving from non-levelized ratemaking to levelized ratemaking will add even more to the transmission costs that these particular customers will have to pay, rather than offsetting benefits that they otherwise would receive from the super-regional rate design.

Finally, the ICC is concerned with IP’s proposal because the use of levelized rates would negatively impact retail competition in Illinois due to the fact that the transmission component of bundled retail rates in Illinois was determined on a net plant basis.³⁷ With bundled retail rates effectively frozen in Illinois through the end of 2004, any increase in the unbundled transmission rate will serve as a disincentive for retail customers to switch to unbundled service. The effect of a transmission rate increase resulting from the switch to levelized transmission rates would be to take much of the competitive pressure off of IP at the retail level.

For all the aforementioned reasons, the ICC respectfully requests that the Commission reject IP’s proposal to utilize levelized ratemaking in this proceeding. As explained, IP’s arguments for levelized ratemaking are either not relevant or not persuasive. Under current circumstances, Commission approval of IP’s request to switch from depreciated non-levelized ratemaking to gross levelized ratemaking would result in artificially high transmission rates that

³⁵ *Id.*

would permit IP to over-recover its costs, and would create an unjust and unreasonable windfall to IP at the expense of transmission ratepayers. Accordingly, the Commission should reject IP's levelized rate proposal.

B. The Commission should initiate a hearing and direct its Staff to investigate the justness and reasonableness of IP's proposed transmission rates.

IP states that it seeks transmission rate changes in this proceeding due to: "increases in transmission plant rate base, increases in transmission expenses, and a greater percentage allocation of certain costs to the transmission function due to the absence of a generation line of business."³⁸ In addition, IP requests Commission authorization of a 14% return on equity allowance in its transmission rates. As explained *supra*, all these elements, in addition to the proposed switch to levelized rates previously discussed, lead to a 54.8% increase over the transmission revenue requirement recently approved by the Commission for IP. In support of this proposed increased revenue requirement, IP provides the testimony of Ms. Peggy Carter (IPC-2), Mr. Lee Lalinsky (IPC-3), Mr. Alan C. Heintz (IPC-4) and Mr. Paul R. Moul (IPC-4).

The ICC declines to address these aspects of IP's transmission rate filing herein because similar testimony has been filed by IP in a proceeding on IP's Delivery Services Tariff ("DST") that is currently pending before the ICC.³⁹ The ICC notes, however, that intervenors (including the ICC Staff) in the ICC proceeding have raised a number of concerns and questions with regard to similar aspects of IP's DST filing. The ICC, therefore, respectfully recommends that the Commission set these matters for hearing and direct its Staff to conduct an investigation into

³⁶ IPC-1 at 10, ln. 8.

³⁷ See, Order, *Illinois Power Co.*, ICC Docket Nos. 99-0120 & 99-0134 (consol.), Appendix A, Schedule 3, ln 3.

³⁸ Transmittal Letter at 3.

³⁹ See, Proposed revisions to delivery services tariff sheets and other sheets, *Illinois Power Co.*, ICC Docket No. 01-0432 (filed June 1, 2001).

IP's transmission rate filing. The Commission's Staff, if it chose, could consult the public record that is available in the ICC proceeding.

III. CONCLUSION

WHEREFORE, for each and all of the forgoing reasons, the ICC respectfully requests that the Commission: 1) reject IP's levelized rate-making proposal; 2) initiate a hearing and direct its Staff to investigate the justness and reasonableness of IP's proposed transmission rates; 3) suspend IP's proposed rates for the maximum period allowed pending their investigation; and 4) grant any and all other appropriate relief.

October 2, 2001

Respectfully submitted,

ILLINOIS COMMERCE COMMISSION

/s/ Sarah A. Naumer

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CERTIFICATE OF SERVICE

I hereby certify that I caused a copy of the foregoing Comments of the Illinois Commerce Commission to be served this day upon each person designated on the official service list compiled by the Secretary in this proceeding in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure.

Dated at Chicago, Illinois, this 2nd day of October, 2001.

/s/ Sarah A. Naumer

Sarah A. Naumer
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